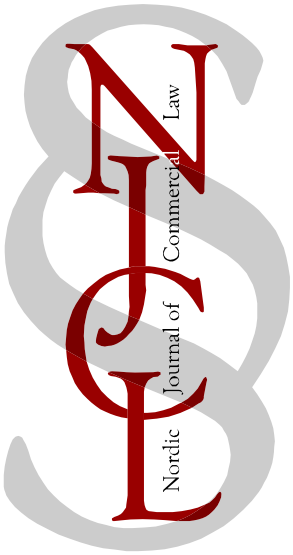

Liability under Pre-contractual Agreements and Their Application under Colombian Law and THE CISG

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I. INTRODUCTION[*] [#]

The purpose of this article is to address the importance of pre -contractual liability in the regulation of contemporary commercial relations in an international context.

In first instance, I will address the regulation of pre-contractual agreements under Colombian domestic law. Second, I will be briefly comparing the application and regulation of pre-contractual liability in Colombian domestic law with its application in American law. Finally, I will address its application under the CISG and I will include a brief comparison of this Convention with Colombian domestic law in respect to this matter.

In addition, I will provide practical examples to illustrate the application of pre-contractual liability under Colombian domestic law and the United Nations Convention on Contracts for the International Sale of Goods (CISG).

II. THE EFFECTS OF PRE CONTRACTUAL AGREEMENTS IN COLOMBIA AND THEIR LIABILITY UNDER THE DOMESTIC LAW

A. Brief Historical Prospective of Pre-Contractual Liability

The law, the doctrine and the jurisprudence in civil law jurisdictions have been regulating issues related to contractual and extra-contractual liability for centuries. However, only in the last century have they turned their attention to pre-contractual liability.

In the early years, there was a dilemma in respect to the recognition of pre-contractual liability because it was understood that this pre-contractual stage did not generate responsibility for the parties because there was not a contract and they had freedom to decide whether they wanted to proceed with the negotiations or simply back out from them. Therefore, any cost spent by the parties in pre-contractual negotiations should been assumed by them if the contract failed to materialize.

[*] The subject matter of this paper is an analysis of the CISG Article 7(1) and its consequences. I also examine the Norwegian implementation of the Convention, how the Norwegian approach relates to the obligations set forth in Article 7(1), and whether that approach is a loyal compliance with those obligations. I further address the problems caused by the Norwegian transformation and how those problems might be solved.

[#] This essay states the law as at 25 January 2007.

Conversely, it had been held by some scholars that pre-contractual agreements caused liability. In their opinion, the parties acquire obligations and rights during the pre-contractual stage. For instance, where two parties have been engaged in extended negotiations for the purchase of a complex business, they ought to owe to each other the obligation to act in good faith. Therefore, after one party has invested a large amount of money studying and researching the business due to its complexity and in reliance on the other party's intention to reach a future agreement, the party ought to be compensated for the economical loss caused by the unjustified withdraw from the negotiations by the other party. The innocent party should be able to demand the relief for the damage caused by such conduct. The innocent party should be allowed to recover the pecuniary loss for the cost of his investment and the loss of opportunities.

These situations were the ones that inspired Rudolph von Jhering to write his monographic on "*culpa in contrahendo*."[1] His goal was to eliminate the injustice that was generated by the impossibility to impose responsibility on the party that without justification and reason withdrew from pre-contractual negotiations causing damages to the other contracting party. It is imperative to indicate that the doctrine of *culpa in contrahendo* is intimately related to the concept of good faith and presupposes fault or negligence by the guilty party.

Precisely, the foundation of the Jhering theory is based on the principle of the good faith that has to be observed between the contracting parties since the beginning of the negotiations.

The doctrine of pre-contractual liability considers the damages that occur as a consequence of the conduct of one of the parties that produced the nullity of the contract or generated the conditions for the cancellation of the negotiations. As mentioned above, the doctrine also considers the damages generated by the intentional and unjustified rupture of the negations by one of the parties.

One example of such conduct is when the seller, knowing that he is not the owner of the goods, sells them to the buyer. In such a situation, the contract will be void because it will be impossible for the performance of the contract since the goods belong to a third party who is not part of the transaction and will claim his ownership of the goods.

Similarly, under the doctrine of pre-contractual liability, a party will be held liable for damages when initiating the previous negotiations with respect to the purchase of a corporation with the intention to gather confidential information of the business and abruptly interrupt the negotiations after the accomplishment of this purpose.

Before the formulation of the doctrine of *culpa in contrahendo*, the law appeared to have ignored pre-contractual stages, more specifically what happened before the formation of the contract, even though, the parties had been involved in extended, complex and expensive negotiations that required them to act in good faith and with due diligence.

[1] Rudolph von Jhering, "Culpa in contrahendo: oder Schadensersatz bei michtigen oder nicht zur Perfektion gelangten Verträgen, Jherings Jahrbücher !V (1861) 1-113.

This historical perspective leads one to think that pre-contractual liability is supported not only in Jhering's theory but also in the principles of good faith, fair dealing and unjust enrichment. It is paramount that once parties enter into contractual negotiations, they owe to each other a relationship of trust and confidence regardless of the negotiation's success or failure.

B. Pre-Contractual Agreements and Their Liability Under Colombian Law

Pre-contractual agreements are intimately connected with what are called "pre contractual relations." Pre-contractual relations arise between the parties who are interested in entering into a contract. These relations arise from the first contacts between the parties until the adoption of a preparatory contract. Such preparatory contracts are termed under the Colombian legislation "*la option o la promesa de contratar*" which means the option or the promise to enter into a contract. This stage is known as the "pre-contractual period." [2]

In our complex economic world, we can find that there are contracts that can be concluded instantaneously according to the nature of their object or their small economic value such as the trading of regular and domestic consumer products which are displayed on supermarket shelves with their prices marked indicating that offers to the public have been made and therefore, it is possible to immediately acquire them for the payment of the price by the consumer. However, there are other kinds of contracts that for their nature and high economic value require a long period of negotiation as well as technical and budget studies by the contracting parties; therefore, the formation of such contracts is progressive. Such contracts, for instance, can be for the construction of complex structures like airports, railroads or the purchase of banks or large corporations.[3]

Moreover, it is in this type of contract where pre-contractual agreements take place. They constitute an important stage where the parties have the opportunity to discuss, learn and discover the advantages and disadvantages of the business. It is in this stage where the parties gather the confidential information of the business such as technical studies, production, marketability of the products, and industrial standards. In this stage, the party interested in the purchase of the business or company may invest a large amount of money as well as time in order to get the information required to make an informed decision in respect to the possible offer and later the conclusion of the contract. These pre-negotiations are called in different civil legislations "*Tratos preliminaries*", "*Conversaciones Previas*" or "*Tratativas*".

Colombian legislation regulates the liability of pre-contractual agreements under Article 863 of the Commercial Code, which provides that the parties shall act in good faith and without fault during pre-contractual negotiations, and that in case of the violation of this provision, the party at fault will be liable for damages caused to the innocent party.

Moreover, Article 872 of the Colombia Commercial Code provides that the celebration and execution of the contract shall be in good faith. As indicated above, this concept has been extended to the pre-contractual stage. Therefore, the parties have the duty to act in good faith

[2] Gabriel Escovar Sanin, Negocios Civiles y Comerciales Tomo II, Dike 379 (1994).
[3] *Id.* at 380.

and without fault, which means that it is not sufficient that they are convinced that they are acting according to the principles of good faith but that they are acting without negligence.

Additionally, Article 830 of the Colombia Commercial Code indicates that a person who abuses his rights and harms another would be liable for the damages caused to the innocent party. This is called "*Abuso del Derecho*" and it is one of the principles that inspired pre-contractual liability. Finally, Article 831 is related to the principle of unjust enrichment.

Accordingly, the importance of the pre-contractual stage is not only related to the protection of the parties against negligence, unfair practices and unjust enrichment, but it is fundamental to the interpretation of the contract. Therefore, the initial acts, agreements, and negotiations between the parties tending toward the celebration and culmination of the contract will indicate their intention to enter into a future contract. For that reason the Colombia Civil Code in Article 1618 indicates that, once the intention of the contracting parties is known, such intention prevails over the literal interpretation of provisions of the contract.

In Colombia, pre-contractual liability does not require the element of "*culpa*" (fault), it only requires the arbitrary rupture of the negotiations; even if such rupture by the contractual party is without fault it will generate liability. The fundamental point is that it goes against commercial equity and good faith. Therefore, the law should not permit one to unfairly withdraw from pre-contractual negotiations without legal consequences in situations in which a party has invested a large amount of money and work searching the business. The importance here it is to protect the parties' patrimonial interest because the frustration of pre-contractual negotiations can caused the same or superior damages as those cause by the breach of the executed contract.

Colombian's Supreme Court has studied the implication of liability for pre-contractual agreements and has encountered some difficulties in the interpretation of the limits of liability and how best to frame the appropriate level of responsibility. The Court's major concern is not to contravene the ambit of freedom of contract.

In addition, the Colombia Supreme Court had held that the compensation for damages caused by one contractual party to the other at the pre-contractual stage is divided into two different categories as follows: "*daño emergente*" and "*lucro cesante*."

"*Daño emergente*" had been defined as the harm suffered by the injured party for the loss of expenses and financial inversions made during the pre-contractual stage. Colombia's legislation considered that these expenses constitute a negative contractual interest for the abrupt and unjustified rupture of pre-contractual negotiations. In consequence, this interest is limited to the amount of the loss of expenses.

This negative interest does not include the expectation interest that the party could have if the contract would have been executed. Moreover, "*daño emergente*" includes the monetary correction.

The interest that emerges from the breach of a valid executed contract is known as "*interés de cumplimiento*" or "*interés positivo*" (positive interests) because its goal is to put the contracting party in the same financial situation that he would have been if the contract had been

performed. The positive interest is the equivalent to the American expectation interest for the breach of a contract. However, the negative interest, which is also know as an "*interés de confianza*" (trust interest), is oriented to compensate the injured party for the loss of expenses that he incurred during pre-contractual negotiation as a consequence of his reliance on the other contracting party interest to continue with the negotiations to finally execute a contract. The negative interest is similar to the American reliance interest for the breach of contract but at a pre-contractual stage.

According to Pedro Lafont Pianetta, who is a Colombian Supreme Court Justice, the negative interest compensates for the loss of expenses, material and moral damage that result from the frustration of pre-contractual agreements. The goal is to bring the injured party to the same financial situation that he was in before he started with pre-contractual negotiations.[4]

Moreover, Gabriel Escovar Sanin indicated that the negative interest has two aspects:

1. The necessity to repair the harm caused by the reliance on the other contractual party, for the trust in her promise
2. The necessity to support and encourage trust and good faith in commercial negotiations.[5]

The understanding of these two aspects is fundamental for the integral interpretation and understanding of the primary goal of pre-contractual liability and its compensation system.

Moreover, the "*lucro cesante*" is defined as a lost of the opportunities that the injured party suffered on reliance of pre-contractual negotiations. In Colombia this is call "*perdida del chance*" (loss of a chance). This situation is presented when an innocent party refused to enter into the negotiations of another contract offered by a third party in reliance of the on-going negotiations with the guilty party. In such case the party at fault has to pay for the loss of opportunities suffered by the injured party.

Colombia Supreme Court Justice Alejandro Bonivento has indicated that the compensation for the breach of pre-contractual negotiations is composed of the "*daño emergente*" and "*lucro cesante*", therefore both interests have to be calculated in order to determine the final compensation.[6]

However, there was a polemic in relation to the amount of damages that should be paid as a consequence of the "*lucro cesante*". The Supreme Court has held that this interest should be measured by the loss of profit that the injured party suffered for the loss of opportunities. For instance, the losses of profits caused when the party refuse to accept another contract proposed by a third party at the same time that he was involved in the negotiations of the frustrated contract.[7]

[4] Corte Suprema de Justicia, Sentnecia de Junio 27 de 1990, M.P: Dr. Pedro Lafont Pianetta.
[5] Sanin, *supra* note 1, at 394
[6] Corte Suprema de Justicia, Sentencia de Noviembre 23 de 1989, M.P: Dr. Jose Alejandro Bonivento Fernandez
[7] Corte Suprema de Justicia, Sentencia de Noviembre 23 de 1989, M.P: Dr. Jose Alejandro Bonivento Fernandez

Finally, pre-contractual liability in Colombia seems to be similar to the reliance interest, and the American doctrine of promissory estoppel in contracts. The concepts of "*daño emergente*" and "*lucro cesante*" have the same inspiration as the principle of the reliance interest: to place the injured party in the same situation as he was before the contract was made. However, the main difference is that such liability is generated in Colombia from the first negotiations and agreements between the parties in pre-contractual stages where there is a tacit agreement between the parties to act in accordance with good faith, fair business, diligence and loyalty.

Also, in Colombia there are three stages in the formation of a contract as follows: the first is pre-contractual agreements or negotiations, the second, is the contractual stage and the last is the post-contractual stage. Each of these stages generates liability to the parties in case of breach.

C. Hypothetical Examples to Illustrate How Pre-contractual Liability is Applied in Colombia

The following are some examples of the situations where pre-contractual liability occurs as defined in Colombia.

a. A company accepted an engineer as a capital partner in the company. The engineer in reliance on the word of the company's President and CEO proceeded to sell some of his properties at a lower price than the commercial price because he wanted to collect the amount of money that he had to pay to become a partner. Also, at the same time, he quit his job in another company. However, a few hours before the execution of the document that recognized him as a partner, the company notified him that they changed the qualifications of admission of the possible partner, and under these new requirements it was impossible for him to become a partner of the company[8].

In this case, the company, even without the existence of a contract, should be responsible for the damages caused to the innocent party because in reliance on their word he left his job and proceeded to sell his properties to respond for the payment that the company required him to make as a capital partner. Here, one party unfairly raised in the other party a hope that a contract will be made.

b. Juan was an old and outstanding client of a bank. He asked for a loan of $500,000.00 dollars (This sum was lower than of the prior sums loaned to him by the bank.) He needed this money for the purchase of some equipment for his company. In compliance with the prior practices with the bank, and the bank holding his mortgages, and the bank's manager's oral confirmation of acceptance of the loan, he proceeded to negotiate for the industrial equipment with the seller and signed a promise of purchase. After the negotiation, he went to the bank to pick up the money for the payment of the equipment. However, he was informed that the credit committee declined his petition for the loan due to a restriction on loans. Juan's financial situation and payments to the institution had been outstanding and did not change from the prior times when he asked the bank for loans. As a consequence, of the negative

[8] Sanin, *Supra* note 1, at 423.

actions of the bank Juan had to pay the amount of a penal clause and suffer enormous detriments in the development and progress of his company.[9]

In this example, the bank's manager made a promise to Juan and broke that promise. Therefore, the bank under the law on pre-contractual agreements, is responsible for the damages caused for their negative action on the loan. The bank's manager knew that, in accordance with prior practices and dealings with Juan, he would commence the negotiations for the equipment and the bank manager's word of acceptance would give Juan a green light to even sign a promise of purchase. Juan acted in reliance on prior practices and the manager's word. In this case, as in the first example, there was a hope that a future contract would be made.

D. Brief Comparison Between Pre-contractual Liability as Applied in Colombia and under American Law

The first example that I gave to illustrate the application of pre-contractual agreements under the Colombian legislation is similar in a way to the case of *Feinberg v. Pfeiffer Co*. where the plaintiff worked for a long time for the defendant and in consideration of his years of services and in gratitude for his hard work, the company made a resolution to recognized an extra payment for the plaintiff upon his retirement (Two hundred dollars for life). The plaintiff, in reliance on this promise, retired. The company made the promised payments for some time until they decided to stop the payments arguing that a promise to make a gift is not binding without consideration and in their case the payment was only a promise and not a standing contract. The court held that in the instant case the plaintiff acted on reliance upon the promise contained in the resolution, and this therefore created an enforceable contract under the doctrine of promissory estoppel. (See § 90 of the Restatement Second of Contracts.) Here the plaintiff, in reliance on the promise, retired. The defendant should have reasonably expected that the plaintiff would act in reliance on their promise; in other words, the defendant induced the plaintiff to retire. Consequently, the court ordered the payments for life.[10]

It is imperative to mention the similarities between the concepts of reliance interest and promissory estoppel in American law and the effects of concept of pre-contractual liability in Colombia. First, under the concepts of reliance interest and the promissory estoppel, the contractual liability arises when one of the parties makes a promise to the other contractual party as a part of the contract. These two concepts presuppose the existence of a valid contract and, as a consequence of it, one party changes his position during the contractual stage in reliance upon the other party promises to perform the contract. Whereas in Colombia pre-contractual liability is imposed as a consequence of the reliance of one party on the other party's promise or inducement to believe that it would be a probable conclusion of a future contract, this liability is generated as a consequence of the rupture of pre-contractual negotiations and the detriment suffered by one party due to the other side's inducement to believe in the possibility of a future contract. Therefore, this kind of liability does not suppose the breach of a valid contract, merely the breach or rupture of the negotiations.

[9] Sanin, *Supra* note 1, at 424 .
[10] *Feinberg v. Pfeiffer Co*. 322 S.W. 2d 163 (MO. Ct. App.1959)

In general. the American legal system does not provide for the concept of *culpa in contrahendo* or pre-contractual liability. However, Puerto Rico has contemplated the doctrine of the *culpa in contrahendo* in its legislation as a consequence of its civil law system. In contrast, the common law states do not recognize the fundamentals of the doctrine of *culpa in contrahendo* and pre-contractual liability.

As I have mentioned before, Colombian's legislation statutorily regulates the figures of *culpa in contrahendo* and, specifically, the liability of pre-contractual agreements.

Colombia's legislation provides remedies for reliance where there has been an arbitrary rupture of pre-contractual negotiations. In consequence, the guilty party will be obligated to pay for the damages cause to the innocent party, who in reliance of the other's word and behavior invests time and money in the initial pre-negotiations stage in order to know the details and gather the information required to make an informed decision before the celebration of the contract.

With respect to the doctrine of the promissory estoppel, Günter Kühne has stated that philosophically it was developed as a consequence of the insufficiency of reliance produce by the bargain and the exchange concept consideration:

"In the United States the promissory estoppel took over the tract to make up for the reliance deficit produced by the bargain and the exchange philosophy of the consideration principle. It became an instrument to enforce gratuitous promises where one, relying on the promise, changed his position and incurred financial losses."[11]

The concept of the doctrine of promissory estoppel is similar to the conception of pre-contractual liability in Colombia in the fact that the main inspiration is to avoid unjust enrichment, to promote fair business practices, and to imposed responsibility on the party who either intentionally or unintentionally made a promise to another and had reason to know that the other party will act in a certain way in reliance on his promise.

The difference is that promissory estoppel operates on a contractual stage, in other words, where a valid contract has been made, and to lock in the offer in a bid case once the contractor has notified the subcontractor that he won the contract.

However, pre-contractual agreements do not require the formation of a valid contract, only the pre-negotiations of it whether or not they come to fruition. Pre-contractual agreements do not require the complete meeting of the minds as is required to obtained relief under the concept of promissory estoppel and the reliance interest in American law.

Pre-contractual agreements only required that the party seeking recovery had reason to conclude from the other party's conduct that a future contract will be made. Here, what is punished is the careless inducement in reliance and the late rupture of negotiations and frustration of

[11] Kühne, Günter, Promissory estoppel and culpa in contrahendo, 10 Tel Aviv University Studies in Law, Tel Aviv 282 (1990).

reliance investment. Consequently, the main point is to recover for the reliance invested during the dealing and the recovery for the economic loss.[12]

Günter Kuhne indicates that in the case of *culpa in contrahendo* and pre-contractual liability, it is possible to conclude that liability of the party is recognized based on two elements:

a. "Violation of a pre-contractual duty, which is the duty in regard to the contractual process before a break-off. (The duty is not to rupture negotiations for other than valid reasons, so the break-of itself caused liability.)
b. The inducement of reliance action to the detriment of the other party. One party changes his position in reliance of the other one promise and behavior."[13]

In respect to the liability imposed through these two elements, it is clear that the parties owed to each other the obligation to act in good faith since the beginning of the negotiations. It is also reasonable to expect the reliance of the other party in the negotiations in changing his position to investigate and gather the prudence information in respect to the business. Consequently, the party might hire attorneys, accountants, engineers and any kind of consultants that he might require to understand and to inform him with respect to the business in negotiation. Therefore, the blameworthy party will be liable for the arbitrary rupture of the negotiations due to the investment made by the other party on reliance on the possible contract, based on the behavior and promises of the other party. In conclusion, it is possible to understand that the liability imposed through these two elements was the natural consequence of its breach.

Moreover, another difference between the Colombian' legislation and the American law in respect to pre-contractual agreements is that the element of good faith is not require in America in pre-contractual stages. In other words, it is not extended to the negotiations. There is not a specific duty to bargain in good faith but there is a duty to be performed in good faith obligation, which is imposed during the contractual stage. Consequently, the Uniform Commercial Code requires merchants to perform in good faith and fair dealing. For instance, in the case of a merchant, the good faith element imposes on him the obligation to observe reasonable commercial standards of fair dealing in the trade and to perform with respect of such standards.[14] While in Colombia, the Commercial Code imposes an obligation on the contractual parties to observe good faith during the pre-contractual stage, Therefore, the blameworthy party would be liable for his breach of such duty. The fundamental point of such provision is that during the pre-contractual stage the parties engaged in the negotiations build between them relationships based on trust similar to the ones that arise in the contractual stage, so they will have to comply with a high standard of care.

In conclusion, pre-contractual liability in Colombia has a high importance in the contractual relations between the parties and therefore the Commercial and Civil Code regulates it extensively. Its goal is to promote good faith and fair dealing during all the contractual stages and as well as to prevent the unjust enrichment of one of the parties to the detriment of the

[12] *Id.* at 282
[13] Kühne, *Supra* note10, at 288
[14] Kessler, Friedrich/Fine, Edith, *Culpa in contrahendo*, Bargaining in Good Faith and Freedom of Contract: A comparative Study, Harvard Law Review, 1964. Pg 408.

other party. The goal of the concept of pre-contractual liability is to restore the damages suffered by one party in reliance on the blameworthy party.

During the negotiation of pre-contractual agreements, some obligations and rights are generated to the parties. The main obligation is to act in good faith, meaning that the parties have to initiate the negotiations with the intention to reach an agreement, and to withdraw as soon as possible, before the other party, in reliance of the negotiations, invests in the research of the business. Also, good faith requires the obligation of reserve which means that information with respect to the business and financial situation of one of the parties ought not to be disclosed if it is confidential. Finally, it requires the obligation of custody and conservation of all the material that has been given to the parties in the course of the negotiations. The withdrawal itself does not cause the liability. There has to be some kind of unfair act such as not intending to reach an agreement and omitting to communicate the determination to he other party, not disclosing trustworthy information, or continuing the negotiations after realizing that the contract will never be concluded.

III. A BRIEF VIEW OF PRE-CONTRACTUAL LIABILITY UNDER THE CISG

We cannot find any provision in the CISG that specifically regulates pre-contractual liability. In this respect, the CISG is silent. However, the application of this concept can nevertheless be inferred from the CISG's general principles, from its provisions and from its interpretation as a whole. The first approach is to look at article 7(1), which addresses the international character of the Convention and its promotion of the principle of good faith in international trade. One then turns to article 7(2) which indicates that, for matters governed by the Convention, but not expressly settled in it, the correct approach is to interpret the matter according to the general principles of the Convention, where such principles are present. Article 8 of the CISG is also highly relevant.

A. Applicability of Pre-Contractual Agreements under the CISG According to Article 7 and Article 8

In my view, in order to have a full understanding of the application of pre-contractual liability under the CISG, one must review the legislative history of article 7 which refers to the good faith principal. I will emphasize in its importance.

According to the legislative records of the Vienna Diplomatic Conference at which the CISG was promulgated, there was a lack of consensus as to the meaning of the principle of good faith provided in article 7. The following are some of the views that were discussed in respect to the inclusion of good faith in international trade:

> *"Colloquy at Diplomatic Conference on Proposal to provide a more specific reference to good faith ("Article [7] [is] not the appropriate place for a reference to a principal of major importance in international trade relations. A separate article [is] required." Proposal rejected" Comments by delegates, some regarding a good faith requirement as present without such a separate article; some not wanting such an article because it would document the existence of a good faith requirement applicable to a contracting parties. OR 257-259,paras. 40-56 [OR=Official Records of the*

United Nations Conference on Contracts for the International Sale of Goods, Vienna 10 March-11 April 1980, A/CONF. 97/19]"[15]

The draft of article 6 that was presented in 1978 was approved as article 7(1) of the official text of the CISG.

The major modifications proposed were presented by Italy and Norway as follows:

"[Italy (A/CONF.97/C.1/L.59):
Delete the words "and the observance of the good faith in international trade" (cf. in this respect the proposed new article 6 [became CISG article 7] ter) and add new sentence:
"questions concerning matters governed by this Convention which are not expressly settle therein shall be settle in conformity with the general principles on which this Convention is based or, in the absence of such principles, by taking account of the national law of each of the parties."]
[Add a new article 6 [became article 7] ter to read as follows:

"In the formation [interpretation] and performance of a contract of sale the parties shall observe the principles of the good faith and international co-operation."]

{Norway (A/CONF.97/C.1/L.28):
Delete the words:
"and the observance of the good faith in international trade"
Article [6] [became article 7]"[16]

During the discussions, Mr. Bonell, who was a member of the Italian delegation indicated that an inclusion of a provision regulating the observance of good faith principle was required in the CISG. Therefore, he supported and proposed the adoption of a separate provision for the regulation of a major principle of good faith. In addition, he stated that his delegation proposed to add a reference to "international cooperation" with the intention to clarify that only those aspects of good faith that were internationally acceptable would apply to the interpretation of the principles under the CISG.[17]

Mr. Rognlien, of Norway, stated that the reference to the principle of good faith should be transferred from article 6 to article 7. He also indicated that the observance of good faith was related to the contract between the parties not to the interpretation of the provisions of the Convention. Therefore, he considered that the reference to good faith should be transferred from article 6 to article 7 (which become article 8 (3) of the CISG). He disagreed with the inclusion of the reference to the international cooperation proposed by Italy.[18]

Miss O'Flynn who represented United Kingdom stated that there was no need to add a new article for the provision of the good faith as it was proposed by Italy. She indicated that the

[15] Article 7 Colloquy, Interpretation of the Convention. Points of view expressed at Vienna Diplomatic Conference, Colloquy on issue related to a good faith: proposal to add to CISG a version of concept of *culpa in contrahendo* (pre-contractual liability): proposal rejected [Official Records 294-295, paras. 77-87] (1980)
[16] *Id.* at 294-295
[17] *Id.*
[18] *Id.*.

meaning of the article involved an uncertain interpretation, the principles of the good faith were not defined, and there was no provision for the application of sanctions that would be applied as a consequence of the failure of one party to act in good faith. In conclusion, she did not support the Italian proposal.[19]

Finally, Mr. Allan Farnsworth, representing the United States, noted that he had a preference for the existing text because the Italian proposal with respect to the application and interpretation of the good faith in an international context was uncertain and dangerous.[20]

The issue related to the prohibition of the parties from departing from their obligation to act in good faith was debated during the discussion related to the principal of good faith. A Canadian proposal read as follows:

> "*Change article 5 [became CISG article 6] to read as follows:*
> *(Canada (A/CONF.97/C.1/L.10):*
> *"(1) The parties may exclude the application of this Convention or, subject to article 11 [became CISG article 12], derogate from or vary the effect of any of its provisions. However, except were the parties have wholly excluded this Convention, the obligation of good faith, diligence and reasonable care prescribe by this Convention may not be excluded by agreement, but the parties may by agreement determinate the standards by which the performance of such obligations are to be measure if such standards are not manifestly unreasonable.]"*[21]

With respect to this issue, Mr. Farnsworth indicated that he did not support the Canadian proposal because it will impose a general obligation of good faith. The majority of the committee was against the Canadian proposal therefore it was not approved.

Finally, the committees discussed a proposal specifically related to pre-contractual liability. The delegates from the German Democratic Republic proposed that a new article on this subject be added to Part II of the Convention. (A/CONF.97/C.1/L.95). The following are some of the comments with respect to this proposal:[22]

> *"78. Mr. PLUNKETT (Ireland) asked whether the proposal envisaged that compensation would be payable even if no contract had been conclude, or if a contract had been conclude, whether it should be payable for something other than a breach of contract.*
> *"79. Mr. MASKOW (German Democratic Republic) replied that it was the essence of his proposal that compensation for expenses could be claim even if there were no contract.*
> *"80. Mr. BONELL (Italy) strongly supported the proposal. His delegation had already submitted a proposal along similar lines. The existing text of the Convention did not take sufficiently into account cases where no contract was concluded but the parties had engaged in detailed negotiations at the pre-contractual stage. Such cases needed regulation because of the risk that one of the parties might abuse its position and act in such a way as to damage the interest of the other party. He thought the drafting of the proposal could be improved, notably by the deletion of the phrase "in the course of the preliminary negotiations", and also by the inclusion of a phrase to*

[19] *Id.*
[20] *Id.*
[21] Official records pp 257-259
[22] *Id.* at 294-295.

cover the situation in which the party had not necessarily had expenses, but had suffered damages. He suggested that an ad hoc working group be set up to produce an agreed text.

"81. Mr. SCHLECHTRIEM (Federal Republic of Germany) sympathized with the object of the proposal but considered it much too far-reaching. Such a general clause might change some of the solutions of the draft, e.g., the provisions dealing with the obligations of the parties or with the revocability of the offer. It would touch on the problem of form requirements and would also affect matters outside the scope of the Convention such as the avoidance of the contract for errors, or the authority of agents.

"82. Mr. BENNETT (Australia) said that he had great difficulty with the proposal. It referred to a failure in duty to take reasonable care, a notion that was not found anywhere else in the Convention. It was not clear what was the standard of reasonable care that was envisaged. The problem was an important one and not merely one of drafting."

As it is reflected in the reading of the opinions, the proposal for pre-contractual liability was highly objected to by members if the committee and was not agreed on.

However, in my opinion, the failure of the approval of the committee to adopt this provision on the regulation of pre-contractual liability under the CSIG was the result of a lack of understanding of the concept by the common law delegations. As I indicated in the first chapter of this article, pre-contractual liability has not been recognized as a part of the contractual law at common law jurisdictions. I think that their major fear is to contravene the principal of freedom of contract. Conversely, the position of the common law jurisdictions, in their effort to protect freedom of contract, is lacking in protection for the contractual parties during pre-contractual negotiations. It is my view that this is a dangerous approach because during pre-contractual negotiations the damages that can result by the unjustified withdraw of the negotiations can be major or equal to the damages caused by the breach of the contract. Therefore, in order to avoid unjust enrichment and honor the principles of good faith and fair dealing from the beginning of the negotiations of a probable contract, the concept of pre-contractual liability should be regarded as a part of contract law.

In addition to its discussion at the Vienna Diplomatic Conference, the concept of pre-contractual liability had been discussed earlier in 1977 at the 9th session where the UNCITRAL Working Group presented its finished draft of the "Formation of the Contract." The draft included the requirement that fair dealing and good faith had to be observed by the parties during the course of the formation of the contract. The German Democratic Republic suggested that a third paragraph be added to the proposal of Hungary (as indicated above such proposal was raised and objected in the Vienna Conference).

In addition, the German Democratic Republic maintained that the observance of fair dealing and good faith was required from the parties during the course of formation of the contract and, if during the preparation and formation of the contract one of the parties violated their duties of customer care the other party had the right to claim compensation for the economic loss.[23]

[23] UNCITRAL Yearbook IX, (1978), A/CN.9/SER.A/1978 pp 66-67; Honnold *Documentary History* pp 298-299.

Furthermore, for some of the drafters the concept of good faith and fair dealing was considered a moral obligation. Therefore, it was highly important that they elevated these principals to the stage of a legal obligation. However, they were concerned that the application of such principles to particular transactions might not lead to the development of a uniformed and coherent case law in international trade because each national court might be influenced by its own legal traditions and beliefs. To conclude, it was the majority opinion that the proposals for pre-contractual liability under the CISG were properly rejected. The view that prevails is that pre-contractual liability is not part of the scope of the Convention. However, there is a minority opinion to the effect that, even though the CISG does not include an express provision dealing with pre-contractual liability, it will be possible for the tribunals to impose its application by the interpretation of the general provision of observance of good faith in international trade and the interpretation of the principals of the Convention as a whole. Respect to this point, Bonell has noted:[24]

> *"The fact that CISG does not have a provision expressly dealing with the pre-contractual liability of the parties for theirs conduct during the negotiations does not necessarily mean that the issue fall outside the scope of the Convention. In fact, pre-contractual liability could simply be – to use the language of Article 7 – one of those questions concerning matters governed by [the] Convention which are not expressly settled in it.... Issues which are outside the scope of the Convention continue to be governed by domestic law while, in the case of simple lacuna, the solution has to be found primarily within the Convention itself, i.e., in conformity with the general principles on which it is based, and only in the absence of such principles, may resort be had to the law applicable by virtue of the relevant conflict of law rules (Cf. Article 7(2))...."*

I agree with Professor Bonell. It is clear that pre-contractual liability should not be considered outside the scope of the CISG. Its application can be possible through the interpretation of the Convention as a whole and in conformity with the application of its general principles. From the analysis of the principles of good faith, and fair dealing in conjunction with the interpretation of the conduct and intention of the parties, it is possible to establish the existence of a pre-contractual liability under the CISG.

Additionally, the application of the principles of good faith and fair dealing has also been recognized by the UNIDROIT Principles. Article 1.7 regulates the general application of the principal of good faith and fair dealing in international trade. Furthermore, the article indicates that the parties cannot "exclude or limit such obligation."[25]

Moreover, Article 2.1.15 which rules on negotiations in bad faith provides:[26]

> *A party is free to negotiate and is not liable for failure to reach an agreement.*
> *However, a party who negotiates or breaks off negotiations in bad faith is liable for the losses caused to the other party.*

[24] Bonnell "Formation of Contracts and Pre-Contractual Liability Under the Vienna Convention on International Sale of Goods" *Formation of Contracts and pre-contractual liability* (ICC Publishing Pub. No. 440/9: 1990) pp 167-171.
[25] Steven J. Burton and Melvin A. Eisenberg, *Contract Law: Selected Sources Materials, UNIDROIT Pinciples,*Thomson West p381 (2006)
[26] Id. at 384.

> *It is bad faith, in particular, for a party to enter into or continue negotiations when intending not to reach an agreement with the other party."*

According to Rodrigo Novoa, it is possible for the courts to find that the adoption of pre-contractual duty to bargain in good faith under the UNIDROIT could be extended to the CISG because the main purpose of the UNIDROIT principles is to provide guidelines for the interpretation and application of the uniform law instruments on international commercial contracts such as the CISG. Therefore, it is probable that the adoption of the pre-contractual duty to bargain in good faith by the UNDROIT principles might persuade a court that this duty is also present under the CISG.[27]

Moreover, Shani Salama considered that article 7(2) of the CISG provides an interpretation tool of the Convention. Therefore, when the courts are filling the gaps encountered in the interpretation of a matter that is not settled in the Convention like the pre-contractual liability they should look at article 7(2) and interpret such matters within the general principles that inspired the Convention. According to Salama the interpretation under article 7(2) required the use of hierarchy methods of interpretation. She indicates that the first approach by a court when it is filling the gaps under the CISG is to look at the provisions and the general principles that inspired the Convention even if the matter is not expressively settled. Second, if the matter is excluded of the scope of the convention, for instance, the liability of the seller for death and personal injury (art 5 CISG), such matter should be resolved according to the rules applicable under the private international law and not the CISG. In consequence, article 7(2) would be inapplicable.[28]

Furthermore, she emphasized that the scholars have not been clear in respect to the interpretation of the definition of "general principles that inspired the CISG. She noted:

> *"The definition of "general principles upon which the Convention is based" falls short of receiving any clear interpretation in the scholarly works. Reference is made to these principles in article 7(2) without further explanation. Jeffrey Hartwing writes that the "general principles are to be derived from the Convention's own provisions". Moreover, Professor Honnold writes that a "particular general principal must be moored to premises that underlie specific provisions of the convention."* [29]

In addition, Salama indicates that the interpretation of the general principles of the Convention should be broader then just limiting their construction only to the general principles that derive from the Convention. Moreover, such construction should not even be limited to the intent of the drafters. The interpretation of the general principles should be broader according to the international character of the Convention article 7(1). In consequence, Salama considered that the courts should look carefully and extensively to the general principles of the Convention because it is a living body capable of changes and adaptation to the new commercial transactions in international commerce. Thus the interpretation of the general principles of the Convention should follow the changes and

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[27] Rodrigo Novoa, *Culpa in contrahendo: A Comparative Law Study: Chilean Law and the United Nations Convention On Contracts For The International Sale Of Goods (CISG),*22 Ariz. J. Int'L & Comp. L. 583. *p 611 (2005)*

[28] Shani Salama, *Pragmatic Responses to Interpretive Impediments: Article 7 of the CISG, An Inter-American Application,* 28 University of Miami Inter-American Law Review p 7-8 (Fall 2006)

[29] *Id* at 8

transactions in international trade. This point of view is consistent with the regulation provided in article 7(2) because one of its goals is to resolve not expressly regulated matters like those that will arise in the future. To conclude, she also supports the view of Professor Guilmard that "promotes that the use of principles of the UNDROIT and PECL as a source of general principles in art 7(2)."[30]

I really like Salama's approach regarding the interpretation of Art 7(2). As I stated before, the pre- contractual liability is within the scope of the CISG .Therefore, following Salama's theory, if a court has to decide a case on pre-contractual liability the first step for the court is to look at the general principles that inspired the CISG because it constitutes and unsettled matter. Thus the interpretation and regulation of the pre-contractual liability will be possible through its principles. Consequently, there is no need to refer and resolve the case according to the private international law. Furthermore, as Salama stated, the interpretation of the general principles of the CISG should be broader according to its international character and not only limited to those derived from the Convention. Consequently, it is possible to conclude that the principles of the UNDROIT and PECL constitute a source of the general principles referred in art 7 (2) and therefore the adoption of pre-contractual duty to bargain in good faith under the UNIDROIT could be extended to the CISG.

Finally, it is imperative to indicate that interpretation of the conduct and intention of the parties is fundamental in the analysis of the application of the pre-contractual liability under the CISG. Article 8 Provides:[31]

> *"(1) For the purposes of the application of this Convention statements made by and other conduct of a party are to be interpreted according to his intent where the other party knew or could not have been unaware what that intent was.*
> *(2) If the preceding paragraph is not applicable, statements made by and other conduct of a party are to be interpreted according to the understanding that a reasonable person of the same kind as the other party would have had in the same circumstances.*
> *(3) In determining the intent of a party or the understanding a reasonable person would have had, due consideration is to be given to all relevant circumstances of the case including the negotiations, any practices which the parties have established between themselves, usages and any subsequent conduct of the parties."*

From the reading of Article 8 of the CISG, it is clear that this provision is not related to the interpretation of the Convention but to the interpretation of the parties' statements, intentions, conducts, usages and practices in light of an international contract of sale of goods.

There are two tests that apply in the interpretation of the party's statements and conduct. The first is the subjective test which indicates that the statements and conducts of the parties are to be understood according with its intent (Article 8(1)) "*where the other party knew or could not have been unaware what that intent was.*" The second is the objective test, which refers to the understanding of the statement and conduct by a reasonable person under the same

[30] Id.
[31] Burton and Eisenberg, *supra note 24, at* 350.

circumstances (Article 8 (2)). The objective test will be applicable when the other party neither knew or nor could have been aware of the intent.

In reference to this article, I would like to emphasize the importance of the interpretation of the conduct, statements and intentions of the parties when they are dealing with pre-contractual negotiations because they will lead one of the parties to rely on and conclude the serious intentions of the other contractual party to a contract. Therefore, the party in reliance on the other party's statements and behaviors will study, research and invest time and money learning the benefits and disadvantages of the future contract. Consequently, if one of the parties abruptly withdraws from the negotiations without justification, it should be liable for the damages caused to the other contractual party.

B. Hypothetical Case to Illustrate the Application of Pre-Contractual Liability Under the CISG.

The following is a hypothetical example that will help to illustrate the application of pre-contractual liability under the CISG:

Wine Co. is a vineyard company located in Italy. The Company is selling its entire production for 2006. The wine is stored in a warehouse located in a distant place. On January 2, 2006, Wine Co. sent information to all its clients stating that it was offering its entire production in the vineyard for 2006 but that the price could not be lower than US $6 per bottle, and its entire production was approximately three million bottles. In addition, Wine Company advised that clients interested in buying the production would have to respond by communication sent to Piero Monestier, CEO of the company no later then January 30, 2006 and that a final contract should be signed by March 30, 2006, after the inspection and testing of the product by interested buyers. The inspection was programmed for February 16, 2006. Three South American firms expressed interest: Concha Co. from Colombia; Toro from Chile and Tinto from Argentina. These three clients traveled to Italy for the inspection. The inspection was held for four days and the clients brought specialists to determine the quality of the wine. The contract was to be awarded to the best proposal twenty days after of the inspection. However, Wine Co. informed its clients ten days after the inspection its refusal to continue with the negotiations. Wine Co. did not give any specific reason to its clients. The company only indicated that due to a policy of the company the negotiation was canceled. Wine Co. knew since January 30, that the negotiation would be canceled due to their contractual obligation with an Italian client. However, the Company did not stop the negotiations and continued with them until the inspection and then, only a few days before the award of the contract, withdrew its proposal. All the countries involved in the negotiations had their relevant places of business in countries that subscribed to the CISG. The damages caused to the clients included the loss of out-of-pocket expenses and the loss of opportunities because they refrained from negotiating with other providers due to the ongoing negotiations with Wine Co.

To establish a case under the concept of pre-contractual liability, four elements are required:[32]

[32] Novoa, *Supra* note 27, at 583

1. *"Preliminary negotiations;*
2. *Breach of the duty to bargain in good faith;*
3. *Causation in fact; and*
4. *Compensable damages."*

The hypothetical case meets these requirements. There were preliminary negotiations, (the requirement of prior inspection of the product and the posterior communication of the offer after 20 days of the inspection), Wine Co. without justification and in bad faith withdrew the negotiations and, as a consequence of the rupture of the negotiations, its clients suffered damages in reliance on its statement and conduct. Wine Co. promoted the preliminary negotiations and did not withdraw the negotiations, as soon as it found out that such a contract would not be concluded. The Company continued with the inspection and let the clients invest money in their travel expenses, salary of experts and caused them to miss other opportunities.

In situations as illustrated in this hypothetical case the application of pre-contractual liability under the CISG should be possible. First, the CISG promotes the general principals of good faith and fair dealing. Therefore, it is possible to conclude that the parties, since the beginning of the negotiation, have the obligation to bargain in good faith and the breach of such obligation will render legal consequences for the damages caused by the breach. Also, it is reasonable to conclude that a party, in reliance on the other party's promises, statements or conduct, will proceed with the due diligence that was required to obtain the conclusion of the contract. For instance, in the hypothetical example any reasonable person in the same situation would have understood that Wine Co. had a serious intention to conclude the negotiations and award the contract to the best offer (Article 8). The parties would never incur such investment in money and work if they did not have an understanding that the proposal sent by Wine Company was serious. Therefore, the intention of the parties was clear. The Wine Company showed an intention to conclude a contract. It would be unfair to conclude that the parties should pay for the cost of the inspection and travel because Wine Company required them to execute the inspection as a condition precedent before the awarding of the contract under circumstances in which. Wine Company knew its intention to withdraw the negotiations but failed to communicate this determination in time. Wine Company did not act according the general principles of good faith and fair dealing that inspire the CISG.

Conversely, I would like to think of the outcome of this case under the analysis of the majority view that held that pre-contractual liability is outside of the scope of the CISG. In their analysis they will probably indicate that the domestic law would apply instead of the CISG because the Convention is silent to this respect.

In my opinion, regarding pre-contractual liability as outside the scope of the CISG will lead to uncertainty and ambiguous interpretations and outcomes because the gap will be fulfilled according to the provisions of the domestic laws. Therefore, if a pre-contractual liability case is decided in common law jurisdictions, it is likely that the parties will not be allowed to recover damages for the unjustified withdraw of pre-contractual negotiations. Conversely, if the same case is resolved by a judge in the civil law jurisdiction, the innocent party will likely be allowed to recover the damages caused in reliance on the other party's intention to conclude a future contract. In consequence, the innocent party will be compensated for the cost of expenses and the lost of opportunities suffered during pre-contractual negotiations.

I believe that the application of domestic law in cases of pre-contractual liability in international contracts would infringe the major principals and goals of the CISG because it will be a lack of unity in the interpretation and outcomes in this matter. Therefore, this conclusion would not honor the uniformity and unity that the Convention pursues.

C. Comparison Between the Application of Pre-Contractual Liability Under the CISG and Colombian Domestic Law

Colombian legislation regulated pre-contractual liability under the Civil and Commercial Code. In contrast, the CISG is silent respect to this matter. The majority of the scholars opine that pre-contractual liability is not within the scope of the CISG. However, I believe that pre-contractual liability is regulated under the CISG and is not outside its scope.

As I indicated before, it is possible to infer its application through the interpretation of its general principles and provisions as a whole. In consequence, the application of pre-contractual liability is possible under the interpretation of the regulations provided in articles 7 and 8 of the CISG.

Article 7 regulates the international character of the Convention and provides for the promotion of good faith in international trade. In addition, this article indicates that where a matter is governed by the Convention but not expressly settled in it, the correct approach is to resolve the matter according to its general principles, where such principles are present.

Similarly, Article 863 of the Colombian Commercial Code sets forth the obligation of the contracting parties to act in good faith and without fault during pre-contractual negotiations and provides that the failure to comply with this obligation will cause the liability of the party at fault.

In addition, Article 872 of the Commercial Code indicates that the celebration and execution of the contracts shall be in good faith.

Moreover, the CISG in Article 8 states that the intention, statements and conduct of the contractual parties should prevail in the interpretation of the contract.

In this aspect, the CISG is also similar to the Colombian legislation because Article 1618 of the Colombian Civil Code states that, once the intention of the contractual party is known, that intention prevails against the literal interpretation of the provisions of the contract.

Finally, both legislations will award damages in reliance to the innocent party. In both cases, the innocent party will be compensated for his out-of-pocket expenses and lost opportunities.

It is also important to mention that, under article 16(2)(b), the CISG regulates promissory estoppel. According to this article, an offer can be withdrawn at any time before its acceptance except when is reasonable to believe that the offeree *in reliance on the offer* acted in a certain way. For instance, the party commenced investment in production, hired some employees and invested in infrastructure, and as a consequence, will suffer damages if the offer is revoked. Thus, he should be allowed to recover damages in reliance. In my view, this protection can be extended to pre-contractual agreements because we are facing similar situations. In pre-

contractual negotiations, we have a party who acted in reliance on the negotiations and as a consequence researched the business, invested money and time learning the opportunities and benefits of the future contract. Therefore, in case of an unjustified withdraw of the negotiations the blameworthy party should be held responsible for the damages caused in reliance.

IV. CONCLUSION

It is true that there is no provision in the CISG that specifically regulates pre-contractual liability. In this respect, the CISG is silent. However, its application can be inferred from its general principles and provisions and from the interpretation of the Convention as a whole. As stated before, the first step is to look to article 7(1), which indicates the international character of the Convention and its promotion of the principal of good faith in international trade. In addition, article 7(2) indicates that where a matter is governed by the Convention but not expressly settled in it the correct approach is to resolve the matter in accordance with the general principles of the Convention where such principles are present.

In my opinion, the intention of the drafters of the CISG was to bind the contracting parties to the compliance of good faith since the beginning of the negotiations of the contract of sale.

Furthermore, one must analyze the intention of the contracting parties according to Article 8. The questions that may arise are: Was there an intention to conclude a contract? Where there promises, statements or conduct that would lead the other contracting party to infer the conclusion of a contract and therefore proceed with the researching the business? If these questions are answered in the affirmative, then it is possible to infer the application of pre-contractual liability due to the reliance of one party in the other's statements and conduct.

Moreover, I think that the UNIDROIT provision on bargaining in good faith could be extended to the CISG because the interpretation of the general principles of the convention should be broader and not only limited to the general principles derived from the Convention. Thus, it could be sustained that the principles of the UNDROIT and PECL can be used as a source of the general principles provided in Article 7(2) CISG as it have been sustained by Salama's theory.

I. INTRODUCTION[*] [#]

The purpose of this article is to address the importance of pre -contractual liability in the regulation of contemporary commercial relations in an international context.

In first instance, I will address the regulation of pre-contractual agreements under Colombian domestic law. Second, I will be briefly comparing the application and regulation of pre-contractual liability in Colombian domestic law with its application in American law. Finally, I will address its application under the CISG and I will include a brief comparison of this Convention with Colombian domestic law in respect to this matter.

In addition, I will provide practical examples to illustrate the application of pre-contractual liability under Colombian domestic law and the United Nations Convention on Contracts for the International Sale of Goods (CISG).

II. THE EFFECTS OF PRE CONTRACTUAL AGREEMENTS IN COLOMBIA AND THEIR LIABILITY UNDER THE DOMESTIC LAW

A. Brief Historical Prospective of Pre-Contractual Liability

The law, the doctrine and the jurisprudence in civil law jurisdictions have been regulating issues related to contractual and extra-contractual liability for centuries. However, only in the last century have they turned their attention to pre-contractual liability.

In the early years, there was a dilemma in respect to the recognition of pre-contractual liability because it was understood that this pre-contractual stage did not generate responsibility for the parties because there was not a contract and they had freedom to decide whether they wanted to proceed with the negotiations or simply back out from them. Therefore, any cost spent by the parties in pre-contractual negotiations should been assumed by them if the contract failed to materialize.

[*] The subject matter of this paper is an analysis of the CISG Article 7(1) and its consequences. I also examine the Norwegian implementation of the Convention, how the Norwegian approach relates to the obligations set forth in Article 7(1), and whether that approach is a loyal compliance with those obligations. I further address the problems caused by the Norwegian transformation and how those problems might be solved.

[#] This essay states the law as at 25 January 2007.

Conversely, it had been held by some scholars that pre-contractual agreements caused liability. In their opinion, the parties acquire obligations and rights during the pre-contractual stage. For instance, where two parties have been engaged in extended negotiations for the purchase of a complex business, they ought to owe to each other the obligation to act in good faith. Therefore, after one party has invested a large amount of money studying and researching the business due to its complexity and in reliance on the other party's intention to reach a future agreement, the party ought to be compensated for the economical loss caused by the unjustified withdraw from the negotiations by the other party. The innocent party should be able to demand the relief for the damage caused by such conduct. The innocent party should be allowed to recover the pecuniary loss for the cost of his investment and the loss of opportunities.

These situations were the ones that inspired Rudolph von Jhering to write his monographic on "*culpa in contrahendo*."[1] His goal was to eliminate the injustice that was generated by the impossibility to impose responsibility on the party that without justification and reason withdrew from pre-contractual negotiations causing damages to the other contracting party. It is imperative to indicate that the doctrine of *culpa in contrahendo* is intimately related to the concept of good faith and presupposes fault or negligence by the guilty party.

Precisely, the foundation of the Jhering theory is based on the principle of the good faith that has to be observed between the contracting parties since the beginning of the negotiations.

The doctrine of pre-contractual liability considers the damages that occur as a consequence of the conduct of one of the parties that produced the nullity of the contract or generated the conditions for the cancellation of the negotiations. As mentioned above, the doctrine also considers the damages generated by the intentional and unjustified rupture of the negations by one of the parties.

One example of such conduct is when the seller, knowing that he is not the owner of the goods, sells them to the buyer. In such a situation, the contract will be void because it will be impossible for the performance of the contract since the goods belong to a third party who is not part of the transaction and will claim his ownership of the goods.

Similarly, under the doctrine of pre-contractual liability, a party will be held liable for damages when initiating the previous negotiations with respect to the purchase of a corporation with the intention to gather confidential information of the business and abruptly interrupt the negotiations after the accomplishment of this purpose.

Before the formulation of the doctrine of *culpa in contrahendo*, the law appeared to have ignored pre-contractual stages, more specifically what happened before the formation of the contract, even though, the parties had been involved in extended, complex and expensive negotiations that required them to act in good faith and with due diligence.

[1] Rudolph von Jhering, "Culpa in contrahendo: oder Schadensersatz bei michtigen oder nicht zur Perfektion gelangten Verträgen, Jherings Jahrbücher !V (1861) 1-113.

This historical perspective leads one to think that pre-contractual liability is supported not only in Jhering's theory but also in the principles of good faith, fair dealing and unjust enrichment. It is paramount that once parties enter into contractual negotiations, they owe to each other a relationship of trust and confidence regardless of the negotiation's success or failure.

B. Pre-Contractual Agreements and Their Liability Under Colombian Law

Pre-contractual agreements are intimately connected with what are called "pre contractual relations." Pre-contractual relations arise between the parties who are interested in entering into a contract. These relations arise from the first contacts between the parties until the adoption of a preparatory contract. Such preparatory contracts are termed under the Colombian legislation "*la option o la promesa de contratar*" which means the option or the promise to enter into a contract. This stage is known as the "pre-contractual period." [2]

In our complex economic world, we can find that there are contracts that can be concluded instantaneously according to the nature of their object or their small economic value such as the trading of regular and domestic consumer products which are displayed on supermarket shelves with their prices marked indicating that offers to the public have been made and therefore, it is possible to immediately acquire them for the payment of the price by the consumer. However, there are other kinds of contracts that for their nature and high economic value require a long period of negotiation as well as technical and budget studies by the contracting parties; therefore, the formation of such contracts is progressive. Such contracts, for instance, can be for the construction of complex structures like airports, railroads or the purchase of banks or large corporations.[3]

Moreover, it is in this type of contract where pre-contractual agreements take place. They constitute an important stage where the parties have the opportunity to discuss, learn and discover the advantages and disadvantages of the business. It is in this stage where the parties gather the confidential information of the business such as technical studies, production, marketability of the products, and industrial standards. In this stage, the party interested in the purchase of the business or company may invest a large amount of money as well as time in order to get the information required to make an informed decision in respect to the possible offer and later the conclusion of the contract. These pre-negotiations are called in different civil legislations "*Tratos preliminaries*", "*Conversaciones Previas*" or "*Tratativas*".

Colombian legislation regulates the liability of pre-contractual agreements under Article 863 of the Commercial Code, which provides that the parties shall act in good faith and without fault during pre-contractual negotiations, and that in case of the violation of this provision, the party at fault will be liable for damages caused to the innocent party.

Moreover, Article 872 of the Colombia Commercial Code provides that the celebration and execution of the contract shall be in good faith. As indicated above, this concept has been extended to the pre-contractual stage. Therefore, the parties have the duty to act in good faith

[2] Gabriel Escovar Sanin, Negocios Civiles y Comerciales Tomo II, Dike 379 (1994).
[3] *Id.* at 380.

and without fault, which means that it is not sufficient that they are convinced that they are acting according to the principles of good faith but that they are acting without negligence.

Additionally, Article 830 of the Colombia Commercial Code indicates that a person who abuses his rights and harms another would be liable for the damages caused to the innocent party. This is called "*Abuso del Derecho*" and it is one of the principles that inspired pre-contractual liability. Finally, Article 831 is related to the principle of unjust enrichment.

Accordingly, the importance of the pre-contractual stage is not only related to the protection of the parties against negligence, unfair practices and unjust enrichment, but it is fundamental to the interpretation of the contract. Therefore, the initial acts, agreements, and negotiations between the parties tending toward the celebration and culmination of the contract will indicate their intention to enter into a future contract. For that reason the Colombia Civil Code in Article 1618 indicates that, once the intention of the contracting parties is known, such intention prevails over the literal interpretation of provisions of the contract.

In Colombia, pre-contractual liability does not require the element of "*culpa*" (fault), it only requires the arbitrary rupture of the negotiations; even if such rupture by the contractual party is without fault it will generate liability. The fundamental point is that it goes against commercial equity and good faith. Therefore, the law should not permit one to unfairly withdraw from pre-contractual negotiations without legal consequences in situations in which a party has invested a large amount of money and work searching the business. The importance here it is to protect the parties' patrimonial interest because the frustration of pre-contractual negotiations can caused the same or superior damages as those cause by the breach of the executed contract.

Colombian's Supreme Court has studied the implication of liability for pre-contractual agreements and has encountered some difficulties in the interpretation of the limits of liability and how best to frame the appropriate level of responsibility. The Court's major concern is not to contravene the ambit of freedom of contract.

In addition, the Colombia Supreme Court had held that the compensation for damages caused by one contractual party to the other at the pre-contractual stage is divided into two different categories as follows: "*daño emergente*" and "*lucro cesante*."

"*Daño emergente*" had been defined as the harm suffered by the injured party for the loss of expenses and financial inversions made during the pre-contractual stage. Colombia's legislation considered that these expenses constitute a negative contractual interest for the abrupt and unjustified rupture of pre-contractual negotiations. In consequence, this interest is limited to the amount of the loss of expenses.

This negative interest does not include the expectation interest that the party could have if the contract would have been executed. Moreover, "*daño emergente*" includes the monetary correction.

The interest that emerges from the breach of a valid executed contract is known as "*interés de cumplimiento*" or "*interés positivo*" (positive interests) because its goal is to put the contracting party in the same financial situation that he would have been if the contract had been

performed. The positive interest is the equivalent to the American expectation interest for the breach of a contract. However, the negative interest, which is also know as an "*interés de confianza*" (trust interest), is oriented to compensate the injured party for the loss of expenses that he incurred during pre-contractual negotiation as a consequence of his reliance on the other contracting party interest to continue with the negotiations to finally execute a contract. The negative interest is similar to the American reliance interest for the breach of contract but at a pre-contractual stage.

According to Pedro Lafont Pianetta, who is a Colombian Supreme Court Justice, the negative interest compensates for the loss of expenses, material and moral damage that result from the frustration of pre-contractual agreements. The goal is to bring the injured party to the same financial situation that he was in before he started with pre-contractual negotiations.[4]

Moreover, Gabriel Escovar Sanin indicated that the negative interest has two aspects:

1. The necessity to repair the harm caused by the reliance on the other contractual party, for the trust in her promise
2. The necessity to support and encourage trust and good faith in commercial negotiations.[5]

The understanding of these two aspects is fundamental for the integral interpretation and understanding of the primary goal of pre-contractual liability and its compensation system.

Moreover, the "*lucro cesante*" is defined as a lost of the opportunities that the injured party suffered on reliance of pre-contractual negotiations. In Colombia this is call "*perdida del chance*" (loss of a chance). This situation is presented when an innocent party refused to enter into the negotiations of another contract offered by a third party in reliance of the on-going negotiations with the guilty party. In such case the party at fault has to pay for the loss of opportunities suffered by the injured party.

Colombia Supreme Court Justice Alejandro Bonivento has indicated that the compensation for the breach of pre-contractual negotiations is composed of the "*daño emergente*" and "*lucro cesante*", therefore both interests have to be calculated in order to determine the final compensation.[6]

However, there was a polemic in relation to the amount of damages that should be paid as a consequence of the "*lucro cesante*". The Supreme Court has held that this interest should be measured by the loss of profit that the injured party suffered for the loss of opportunities. For instance, the losses of profits caused when the party refuse to accept another contract proposed by a third party at the same time that he was involved in the negotiations of the frustrated contract.[7]

[4] Corte Suprema de Justicia, Sentnecia de Junio 27 de 1990, M.P: Dr. Pedro Lafont Pianetta.
[5] Sanin, *supra* note 1, at 394
[6] Corte Suprema de Justicia, Sentencia de Noviembre 23 de 1989, M.P: Dr. Jose Alejandro Bonivento Fernandez
[7] Corte Suprema de Justicia, Sentencia de Noviembre 23 de 1989, M.P: Dr. Jose Alejandro Bonivento Fernandez

Finally, pre-contractual liability in Colombia seems to be similar to the reliance interest, and the American doctrine of promissory estoppel in contracts. The concepts of "*daño emergente*" and "*lucro cesante*" have the same inspiration as the principle of the reliance interest: to place the injured party in the same situation as he was before the contract was made. However, the main difference is that such liability is generated in Colombia from the first negotiations and agreements between the parties in pre-contractual stages where there is a tacit agreement between the parties to act in accordance with good faith, fair business, diligence and loyalty.

Also, in Colombia there are three stages in the formation of a contract as follows: the first is pre-contractual agreements or negotiations, the second, is the contractual stage and the last is the post-contractual stage. Each of these stages generates liability to the parties in case of breach.

C. Hypothetical Examples to Illustrate How Pre-contractual Liability is Applied in Colombia

The following are some examples of the situations where pre-contractual liability occurs as defined in Colombia.

a. A company accepted an engineer as a capital partner in the company. The engineer in reliance on the word of the company's President and CEO proceeded to sell some of his properties at a lower price than the commercial price because he wanted to collect the amount of money that he had to pay to become a partner. Also, at the same time, he quit his job in another company. However, a few hours before the execution of the document that recognized him as a partner, the company notified him that they changed the qualifications of admission of the possible partner, and under these new requirements it was impossible for him to become a partner of the company[8].

In this case, the company, even without the existence of a contract, should be responsible for the damages caused to the innocent party because in reliance on their word he left his job and proceeded to sell his properties to respond for the payment that the company required him to make as a capital partner. Here, one party unfairly raised in the other party a hope that a contract will be made.

b. Juan was an old and outstanding client of a bank. He asked for a loan of $500,000.00 dollars (This sum was lower than of the prior sums loaned to him by the bank.) He needed this money for the purchase of some equipment for his company. In compliance with the prior practices with the bank, and the bank holding his mortgages, and the bank's manager's oral confirmation of acceptance of the loan, he proceeded to negotiate for the industrial equipment with the seller and signed a promise of purchase. After the negotiation, he went to the bank to pick up the money for the payment of the equipment. However, he was informed that the credit committee declined his petition for the loan due to a restriction on loans. Juan's financial situation and payments to the institution had been outstanding and did not change from the prior times when he asked the bank for loans. As a consequence, of the negative

[8] Sanin, *Supra* note 1, at 423.

actions of the bank Juan had to pay the amount of a penal clause and suffer enormous detriments in the development and progress of his company.[9]

In this example, the bank's manager made a promise to Juan and broke that promise. Therefore, the bank under the law on pre-contractual agreements, is responsible for the damages caused for their negative action on the loan. The bank's manager knew that, in accordance with prior practices and dealings with Juan, he would commence the negotiations for the equipment and the bank manager's word of acceptance would give Juan a green light to even sign a promise of purchase. Juan acted in reliance on prior practices and the manager's word. In this case, as in the first example, there was a hope that a future contract would be made.

D. Brief Comparison Between Pre-contractual Liability as Applied in Colombia and under American Law

The first example that I gave to illustrate the application of pre-contractual agreements under the Colombian legislation is similar in a way to the case of *Feinberg v. Pfeiffer Co.* where the plaintiff worked for a long time for the defendant and in consideration of his years of services and in gratitude for his hard work, the company made a resolution to recognized an extra payment for the plaintiff upon his retirement (Two hundred dollars for life). The plaintiff, in reliance on this promise, retired. The company made the promised payments for some time until they decided to stop the payments arguing that a promise to make a gift is not binding without consideration and in their case the payment was only a promise and not a standing contract. The court held that in the instant case the plaintiff acted on reliance upon the promise contained in the resolution, and this therefore created an enforceable contract under the doctrine of promissory estoppel. (See § 90 of the Restatement Second of Contracts.) Here the plaintiff, in reliance on the promise, retired. The defendant should have reasonably expected that the plaintiff would act in reliance on their promise; in other words, the defendant induced the plaintiff to retire. Consequently, the court ordered the payments for life.[10]

It is imperative to mention the similarities between the concepts of reliance interest and promissory estoppel in American law and the effects of concept of pre-contractual liability in Colombia. First, under the concepts of reliance interest and the promissory estoppel, the contractual liability arises when one of the parties makes a promise to the other contractual party as a part of the contract. These two concepts presuppose the existence of a valid contract and, as a consequence of it, one party changes his position during the contractual stage in reliance upon the other party promises to perform the contract. Whereas in Colombia pre-contractual liability is imposed as a consequence of the reliance of one party on the other party's promise or inducement to believe that it would be a probable conclusion of a future contract, this liability is generated as a consequence of the rupture of pre-contractual negotiations and the detriment suffered by one party due to the other side's inducement to believe in the possibility of a future contract. Therefore, this kind of liability does not suppose the breach of a valid contract, merely the breach or rupture of the negotiations.

[9] Sanin, *Supra* note 1, at 424 .
[10] *Feinberg v. Pfeiffer Co.* 322 S.W. 2d 163 (MO. Ct. App.1959)

In general. the American legal system does not provide for the concept of *culpa in contrahendo* or pre-contractual liability. However, Puerto Rico has contemplated the doctrine of the *culpa in contrahendo* in its legislation as a consequence of its civil law system. In contrast, the common law states do not recognize the fundamentals of the doctrine of *culpa in contrahendo* and pre-contractual liability.

As I have mentioned before, Colombian's legislation statutorily regulates the figures of *culpa in contrahendo* and, specifically, the liability of pre-contractual agreements.

Colombia's legislation provides remedies for reliance where there has been an arbitrary rupture of pre-contractual negotiations. In consequence, the guilty party will be obligated to pay for the damages cause to the innocent party, who in reliance of the other's word and behavior invests time and money in the initial pre-negotiations stage in order to know the details and gather the information required to make an informed decision before the celebration of the contract.

With respect to the doctrine of the promissory estoppel, Günter Kühne has stated that philosophically it was developed as a consequence of the insufficiency of reliance produce by the bargain and the exchange concept consideration:

"In the United States the promissory estoppel took over the tract to make up for the reliance deficit produced by the bargain and the exchange philosophy of the consideration principle. It became an instrument to enforce gratuitous promises where one, relying on the promise, changed his position and incurred financial losses."[11]

The concept of the doctrine of promissory estoppel is similar to the conception of pre-contractual liability in Colombia in the fact that the main inspiration is to avoid unjust enrichment, to promote fair business practices, and to imposed responsibility on the party who either intentionally or unintentionally made a promise to another and had reason to know that the other party will act in a certain way in reliance on his promise.

The difference is that promissory estoppel operates on a contractual stage, in other words, where a valid contract has been made, and to lock in the offer in a bid case once the contractor has notified the subcontractor that he won the contract.

However, pre-contractual agreements do not require the formation of a valid contract, only the pre-negotiations of it whether or not they come to fruition. Pre-contractual agreements do not require the complete meeting of the minds as is required to obtained relief under the concept of promissory estoppel and the reliance interest in American law.

Pre-contractual agreements only required that the party seeking recovery had reason to conclude from the other party's conduct that a future contract will be made. Here, what is punished is the careless inducement in reliance and the late rupture of negotiations and frustration of

[11] Kühne, Günter, Promissory estoppel and culpa in contrahendo, 10 Tel Aviv University Studies in Law, Tel Aviv 282 (1990).

reliance investment. Consequently, the main point is to recover for the reliance invested during the dealing and the recovery for the economic loss.[12]

Günter Kuhne indicates that in the case of *culpa in contrahendo* and pre-contractual liability, it is possible to conclude that liability of the party is recognized based on two elements:

a. "Violation of a pre-contractual duty, which is the duty in regard to the contractual process before a break-off. (The duty is not to rupture negotiations for other than valid reasons, so the break-of itself caused liability.)
b. The inducement of reliance action to the detriment of the other party. One party changes his position in reliance of the other one promise and behavior."[13]

In respect to the liability imposed through these two elements, it is clear that the parties owed to each other the obligation to act in good faith since the beginning of the negotiations. It is also reasonable to expect the reliance of the other party in the negotiations in changing his position to investigate and gather the prudence information in respect to the business. Consequently, the party might hire attorneys, accountants, engineers and any kind of consultants that he might require to understand and to inform him with respect to the business in negotiation. Therefore, the blameworthy party will be liable for the arbitrary rupture of the negotiations due to the investment made by the other party on reliance on the possible contract, based on the behavior and promises of the other party. In conclusion, it is possible to understand that the liability imposed through these two elements was the natural consequence of its breach.

Moreover, another difference between the Colombian' legislation and the American law in respect to pre-contractual agreements is that the element of good faith is not require in America in pre-contractual stages. In other words, it is not extended to the negotiations. There is not a specific duty to bargain in good faith but there is a duty to be performed in good faith obligation, which is imposed during the contractual stage. Consequently, the Uniform Commercial Code requires merchants to perform in good faith and fair dealing. For instance, in the case of a merchant, the good faith element imposes on him the obligation to observe reasonable commercial standards of fair dealing in the trade and to perform with respect of such standards.[14] While in Colombia, the Commercial Code imposes an obligation on the contractual parties to observe good faith during the pre-contractual stage, Therefore, the blameworthy party would be liable for his breach of such duty. The fundamental point of such provision is that during the pre-contractual stage the parties engaged in the negotiations build between them relationships based on trust similar to the ones that arise in the contractual stage, so they will have to comply with a high standard of care.

In conclusion, pre-contractual liability in Colombia has a high importance in the contractual relations between the parties and therefore the Commercial and Civil Code regulates it extensively. Its goal is to promote good faith and fair dealing during all the contractual stages and as well as to prevent the unjust enrichment of one of the parties to the detriment of the

[12] *Id.* at 282
[13] Kühne, *Supra* note10, at 288
[14] Kessler, Friedrich/Fine, Edith, *Culpa in contrahendo*, Bargaining in Good Faith and Freedom of Contract: A comparative Study, Harvard Law Review, 1964. Pg 408.

other party. The goal of the concept of pre-contractual liability is to restore the damages suffered by one party in reliance on the blameworthy party.

During the negotiation of pre-contractual agreements, some obligations and rights are generated to the parties. The main obligation is to act in good faith, meaning that the parties have to initiate the negotiations with the intention to reach an agreement, and to withdraw as soon as possible, before the other party, in reliance of the negotiations, invests in the research of the business. Also, good faith requires the obligation of reserve which means that information with respect to the business and financial situation of one of the parties ought not to be disclosed if it is confidential. Finally, it requires the obligation of custody and conservation of all the material that has been given to the parties in the course of the negotiations. The withdrawal itself does not cause the liability. There has to be some kind of unfair act such as not intending to reach an agreement and omitting to communicate the determination to he other party, not disclosing trustworthy information, or continuing the negotiations after realizing that the contract will never be concluded.

III. A BRIEF VIEW OF PRE-CONTRACTUAL LIABILITY UNDER THE CISG

We cannot find any provision in the CISG that specifically regulates pre-contractual liability. In this respect, the CISG is silent. However, the application of this concept can nevertheless be inferred from the CISG's general principles, from its provisions and from its interpretation as a whole. The first approach is to look at article 7(1), which addresses the international character of the Convention and its promotion of the principle of good faith in international trade. One then turns to article 7(2) which indicates that, for matters governed by the Convention, but not expressly settled in it, the correct approach is to interpret the matter according to the general principles of the Convention, where such principles are present. Article 8 of the CISG is also highly relevant.

A. Applicability of Pre-Contractual Agreements under the CISG According to Article 7 and Article 8

In my view, in order to have a full understanding of the application of pre-contractual liability under the CISG, one must review the legislative history of article 7 which refers to the good faith principal. I will emphasize in its importance.

According to the legislative records of the Vienna Diplomatic Conference at which the CISG was promulgated, there was a lack of consensus as to the meaning of the principle of good faith provided in article 7. The following are some of the views that were discussed in respect to the inclusion of good faith in international trade:

> *"Colloquy at Diplomatic Conference on Proposal to provide a more specific reference to good faith ("Article [7] [is] not the appropriate place for a reference to a principal of major importance in international trade relations. A separate article [is] required." Proposal rejected" Comments by delegates, some regarding a good faith requirement as present without such a separate article; some not wanting such an article because it would document the existence of a good faith requirement applicable to a contracting parties. OR 257-259,paras. 40-56 [OR=Official Records of the*

United Nations Conference on Contracts for the International Sale of Goods, Vienna 10 March-11 April 1980, A/CONF. 97/19]"[15]

The draft of article 6 that was presented in 1978 was approved as article 7(1) of the official text of the CISG.

The major modifications proposed were presented by Italy and Norway as follows:

"[Italy (A/CONF.97/C.1/L.59):
Delete the words "and the observance of the good faith in international trade" (cf. in this respect the proposed new article 6 [became CISG article 7] ter) and add new sentence:
"questions concerning matters governed by this Convention which are not expressly settle therein shall be settle in conformity with the general principles on which this Convention is based or, in the absence of such principles, by taking account of the national law of each of the parties."]
[Add a new article 6 [became article 7] ter to read as follows:

"In the formation [interpretation] and performance of a contract of sale the parties shall observe the principles of the good faith and international co-operation."]

{Norway (A/CONF.97/C.1/L.28):
Delete the words:
"and the observance of the good faith in international trade"
Article [6] [became article 7]"[16]

During the discussions, Mr. Bonell, who was a member of the Italian delegation indicated that an inclusion of a provision regulating the observance of good faith principle was required in the CISG. Therefore, he supported and proposed the adoption of a separate provision for the regulation of a major principle of good faith. In addition, he stated that his delegation proposed to add a reference to "international cooperation" with the intention to clarify that only those aspects of good faith that were internationally acceptable would apply to the interpretation of the principles under the CISG.[17]

Mr. Rognlien, of Norway, stated that the reference to the principle of good faith should be transferred from article 6 to article 7. He also indicated that the observance of good faith was related to the contract between the parties not to the interpretation of the provisions of the Convention. Therefore, he considered that the reference to good faith should be transferred from article 6 to article 7 (which become article 8 (3) of the CISG). He disagreed with the inclusion of the reference to the international cooperation proposed by Italy.[18]

Miss O'Flynn who represented United Kingdom stated that there was no need to add a new article for the provision of the good faith as it was proposed by Italy. She indicated that the

[15] Article 7 Colloquy, Interpretation of the Convention. Points of view expressed at Vienna Diplomatic Conference, Colloquy on issue related to a good faith: proposal to add to CISG a version of concept of *culpa in contrahendo* (pre-contractual liability): proposal rejected [Official Records 294-295, paras. 77-87] (1980)
[16] *Id.* at 294-295
[17] *Id.*
[18] *Id.*.

meaning of the article involved an uncertain interpretation, the principles of the good faith were not defined, and there was no provision for the application of sanctions that would be applied as a consequence of the failure of one party to act in good faith. In conclusion, she did not support the Italian proposal.[19]

Finally, Mr. Allan Farnsworth, representing the United States, noted that he had a preference for the existing text because the Italian proposal with respect to the application and interpretation of the good faith in an international context was uncertain and dangerous.[20]

The issue related to the prohibition of the parties from departing from their obligation to act in good faith was debated during the discussion related to the principal of good faith. A Canadian proposal read as follows:

> "*Change article 5 [became CISG article 6] to read as follows:*
> *(Canada (A/CONF.97/C.1/L.10):*
> *"(1) The parties may exclude the application of this Convention or, subject to article 11 [became CISG article 12], derogate from or vary the effect of any of its provisions. However, except were the parties have wholly excluded this Convention, the obligation of good faith, diligence and reasonable care prescribe by this Convention may not be excluded by agreement, but the parties may by agreement determinate the standards by which the performance of such obligations are to be measure if such standards are not manifestly unreasonable.]"*[21]

With respect to this issue, Mr. Farnsworth indicated that he did not support the Canadian proposal because it will impose a general obligation of good faith. The majority of the committee was against the Canadian proposal therefore it was not approved.

Finally, the committees discussed a proposal specifically related to pre-contractual liability. The delegates from the German Democratic Republic proposed that a new article on this subject be added to Part II of the Convention. (A/CONF.97/C.1/L.95). The following are some of the comments with respect to this proposal:[22]

> *"78. Mr. PLUNKETT (Ireland) asked whether the proposal envisaged that compensation would be payable even if no contract had been conclude, or if a contract had been conclude, whether it should be payable for something other than a breach of contract.*
> *"79. Mr. MASKOW (German Democratic Republic) replied that it was the essence of his proposal that compensation for expenses could be claim even if there were no contract.*
> *"80. Mr. BONELL (Italy) strongly supported the proposal. His delegation had already submitted a proposal along similar lines. The existing text of the Convention did not take sufficiently into account cases where no contract was concluded but the parties had engaged in detailed negotiations at the pre-contractual stage. Such cases needed regulation because of the risk that one of the parties might abuse its position and act in such a way as to damage the interest of the other party. He thought the drafting of the proposal could be improved, notably by the deletion of the phrase "in the course of the preliminary negotiations", and also by the inclusion of a phrase to*

[19] *Id.*
[20] *Id.*
[21] Official records pp 257-259
[22] *Id.* at 294-295.

cover the situation in which the party had not necessarily had expenses, but had suffered damages. He suggested that an ad hoc working group be set up to produce an agreed text.

"81. Mr. SCHLECHTRIEM (Federal Republic of Germany) sympathized with the object of the proposal but considered it much too far-reaching. Such a general clause might change some of the solutions of the draft, e.g., the provisions dealing with the obligations of the parties or with the revocability of the offer. It would touch on the problem of form requirements and would also affect matters outside the scope of the Convention such as the avoidance of the contract for errors, or the authority of agents.

"82. Mr. BENNETT (Australia) said that he had great difficulty with the proposal. It referred to a failure in duty to take reasonable care, a notion that was not found anywhere else in the Convention. It was not clear what was the standard of reasonable care that was envisaged. The problem was an important one and not merely one of drafting."

As it is reflected in the reading of the opinions, the proposal for pre-contractual liability was highly objected to by members if the committee and was not agreed on.

However, in my opinion, the failure of the approval of the committee to adopt this provision on the regulation of pre-contractual liability under the CSIG was the result of a lack of understanding of the concept by the common law delegations. As I indicated in the first chapter of this article, pre-contractual liability has not been recognized as a part of the contractual law at common law jurisdictions. I think that their major fear is to contravene the principal of freedom of contract. Conversely, the position of the common law jurisdictions, in their effort to protect freedom of contract, is lacking in protection for the contractual parties during pre-contractual negotiations. It is my view that this is a dangerous approach because during pre-contractual negotiations the damages that can result by the unjustified withdraw of the negotiations can be major or equal to the damages caused by the breach of the contract. Therefore, in order to avoid unjust enrichment and honor the principles of good faith and fair dealing from the beginning of the negotiations of a probable contract, the concept of pre-contractual liability should be regarded as a part of contract law.

In addition to its discussion at the Vienna Diplomatic Conference, the concept of pre-contractual liability had been discussed earlier in 1977 at the 9th session where the UNCITRAL Working Group presented its finished draft of the "Formation of the Contract." The draft included the requirement that fair dealing and good faith had to be observed by the parties during the course of the formation of the contract. The German Democratic Republic suggested that a third paragraph be added to the proposal of Hungary (as indicated above such proposal was raised and objected in the Vienna Conference).

In addition, the German Democratic Republic maintained that the observance of fair dealing and good faith was required from the parties during the course of formation of the contract and, if during the preparation and formation of the contract one of the parties violated their duties of customer care the other party had the right to claim compensation for the economic loss.[23]

[23] UNCITRAL Yearbook IX, (1978), A/CN.9/SER.A/1978 pp 66-67; Honnold *Documentary History* pp 298-299.

Furthermore, for some of the drafters the concept of good faith and fair dealing was considered a moral obligation. Therefore, it was highly important that they elevated these principals to the stage of a legal obligation. However, they were concerned that the application of such principles to particular transactions might not lead to the development of a uniformed and coherent case law in international trade because each national court might be influenced by its own legal traditions and beliefs. To conclude, it was the majority opinion that the proposals for pre-contractual liability under the CISG were properly rejected. The view that prevails is that pre-contractual liability is not part of the scope of the Convention. However, there is a minority opinion to the effect that, even though the CISG does not include an express provision dealing with pre-contractual liability, it will be possible for the tribunals to impose its application by the interpretation of the general provision of observance of good faith in international trade and the interpretation of the principals of the Convention as a whole. Respect to this point, Bonell has noted:[24]

> *"The fact that CISG does not have a provision expressly dealing with the pre-contractual liability of the parties for theirs conduct during the negotiations does not necessarily mean that the issue fall outside the scope of the Convention. In fact, pre-contractual liability could simply be – to use the language of Article 7 – one of those questions concerning matters governed by [the] Convention which are not expressly settled in it.... Issues which are outside the scope of the Convention continue to be governed by domestic law while, in the case of simple lacuna, the solution has to be found primarily within the Convention itself, i.e., in conformity with the general principles on which it is based, and only in the absence of such principles, may resort be had to the law applicable by virtue of the relevant conflict of law rules (Cf. Article 7(2))...."*

I agree with Professor Bonell. It is clear that pre-contractual liability should not be considered outside the scope of the CISG. Its application can be possible through the interpretation of the Convention as a whole and in conformity with the application of its general principles. From the analysis of the principles of good faith, and fair dealing in conjunction with the interpretation of the conduct and intention of the parties, it is possible to establish the existence of a pre-contractual liability under the CISG.

Additionally, the application of the principles of good faith and fair dealing has also been recognized by the UNIDROIT Principles. Article 1.7 regulates the general application of the principal of good faith and fair dealing in international trade. Furthermore, the article indicates that the parties cannot "exclude or limit such obligation."[25]

Moreover, Article 2.1.15 which rules on negotiations in bad faith provides:[26]

> *A party is free to negotiate and is not liable for failure to reach an agreement.*
> *However, a party who negotiates or breaks off negotiations in bad faith is liable for the losses caused to the other party.*

[24] Bonnell "Formation of Contracts and Pre-Contractual Liability Under the Vienna Convention on International Sale of Goods" *Formation of Contracts and pre-contractual liability* (ICC Publishing Pub. No. 440/9: 1990) pp 167-171.
[25] Steven J. Burton and Melvin A. Eisenberg, *Contract Law: Selected Sources Materials, UNIDROIT Pinciples,*Thomson West p381 (2006)
[26] Id. at 384.

> *It is bad faith, in particular, for a party to enter into or continue negotiations when intending not to reach an agreement with the other party."*

According to Rodrigo Novoa, it is possible for the courts to find that the adoption of pre-contractual duty to bargain in good faith under the UNIDROIT could be extended to the CISG because the main purpose of the UNIDROIT principles is to provide guidelines for the interpretation and application of the uniform law instruments on international commercial contracts such as the CISG. Therefore, it is probable that the adoption of the pre-contractual duty to bargain in good faith by the UNDROIT principles might persuade a court that this duty is also present under the CISG.[27]

Moreover, Shani Salama considered that article 7(2) of the CISG provides an interpretation tool of the Convention. Therefore, when the courts are filling the gaps encountered in the interpretation of a matter that is not settled in the Convention like the pre-contractual liability they should look at article 7(2) and interpret such matters within the general principles that inspired the Convention. According to Salama the interpretation under article 7(2) required the use of hierarchy methods of interpretation. She indicates that the first approach by a court when it is filling the gaps under the CISG is to look at the provisions and the general principles that inspired the Convention even if the matter is not expressively settled. Second, if the matter is excluded of the scope of the convention, for instance, the liability of the seller for death and personal injury (art 5 CISG), such matter should be resolved according to the rules applicable under the private international law and not the CISG. In consequence, article 7(2) would be inapplicable.[28]

Furthermore, she emphasized that the scholars have not been clear in respect to the interpretation of the definition of "general principles that inspired the CISG. She noted:

> *"The definition of "general principles upon which the Convention is based" falls short of receiving any clear interpretation in the scholarly works. Reference is made to these principles in article 7(2) without further explanation. Jeffrey Hartwing writes that the "general principles are to be derived from the Convention's own provisions". Moreover, Professor Honnold writes that a "particular general principal must be moored to premises that underlie specific provisions of the convention."* [29]

In addition, Salama indicates that the interpretation of the general principles of the Convention should be broader then just limiting their construction only to the general principles that derive from the Convention. Moreover, such construction should not even be limited to the intent of the drafters. The interpretation of the general principles should be broader according to the international character of the Convention article 7(1). In consequence, Salama considered that the courts should look carefully and extensively to the general principles of the Convention because it is a living body capable of changes and adaptation to the new commercial transactions in international commerce. Thus the interpretation of the general principles of the Convention should follow the changes and

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[27] Rodrigo Novoa, *Culpa in contrahendo: A Comparative Law Study: Chilean Law and the United Nations Convention On Contracts For The International Sale Of Goods (CISG),*22 Ariz. J. Int'L & Comp. L. 583. *p 611 (2005)*

[28] Shani Salama, *Pragmatic Responses to Interpretive Impediments: Article 7 of the CISG, An Inter-American Application,* 28 University of Miami Inter-American Law Review p 7-8 (Fall 2006)

[29] *Id* at 8

transactions in international trade. This point of view is consistent with the regulation provided in article 7(2) because one of its goals is to resolve not expressly regulated matters like those that will arise in the future. To conclude, she also supports the view of Professor Guilmard that "promotes that the use of principles of the UNDROIT and PECL as a source of general principles in art 7(2)."[30]

I really like Salama's approach regarding the interpretation of Art 7(2). As I stated before, the pre- contractual liability is within the scope of the CISG .Therefore, following Salama's theory, if a court has to decide a case on pre-contractual liability the first step for the court is to look at the general principles that inspired the CISG because it constitutes and unsettled matter. Thus the interpretation and regulation of the pre-contractual liability will be possible through its principles. Consequently, there is no need to refer and resolve the case according to the private international law. Furthermore, as Salama stated, the interpretation of the general principles of the CISG should be broader according to its international character and not only limited to those derived from the Convention. Consequently, it is possible to conclude that the principles of the UNDROIT and PECL constitute a source of the general principles referred in art 7 (2) and therefore the adoption of pre-contractual duty to bargain in good faith under the UNIDROIT could be extended to the CISG.

Finally, it is imperative to indicate that interpretation of the conduct and intention of the parties is fundamental in the analysis of the application of the pre-contractual liability under the CISG. Article 8 Provides:[31]

> *"(1) For the purposes of the application of this Convention statements made by and other conduct of a party are to be interpreted according to his intent where the other party knew or could not have been unaware what that intent was.*
> *(2) If the preceding paragraph is not applicable, statements made by and other conduct of a party are to be interpreted according to the understanding that a reasonable person of the same kind as the other party would have had in the same circumstances.*
> *(3) In determining the intent of a party or the understanding a reasonable person would have had, due consideration is to be given to all relevant circumstances of the case including the negotiations, any practices which the parties have established between themselves, usages and any subsequent conduct of the parties."*

From the reading of Article 8 of the CISG, it is clear that this provision is not related to the interpretation of the Convention but to the interpretation of the parties' statements, intentions, conducts, usages and practices in light of an international contract of sale of goods.

There are two tests that apply in the interpretation of the party's statements and conduct. The first is the subjective test which indicates that the statements and conducts of the parties are to be understood according with its intent (Article 8(1)) "*where the other party knew or could not have been unaware what that intent was.*" The second is the objective test, which refers to the understanding of the statement and conduct by a reasonable person under the same

[30] Id.
[31] Burton and Eisenberg, *supra note 24, at* 350.

circumstances (Article 8 (2)). The objective test will be applicable when the other party neither knew or nor could have been aware of the intent.

In reference to this article, I would like to emphasize the importance of the interpretation of the conduct, statements and intentions of the parties when they are dealing with pre-contractual negotiations because they will lead one of the parties to rely on and conclude the serious intentions of the other contractual party to a contract. Therefore, the party in reliance on the other party's statements and behaviors will study, research and invest time and money learning the benefits and disadvantages of the future contract. Consequently, if one of the parties abruptly withdraws from the negotiations without justification, it should be liable for the damages caused to the other contractual party.

B. Hypothetical Case to Illustrate the Application of Pre-Contractual Liability Under the CISG.

The following is a hypothetical example that will help to illustrate the application of pre-contractual liability under the CISG:

Wine Co. is a vineyard company located in Italy. The Company is selling its entire production for 2006. The wine is stored in a warehouse located in a distant place. On January 2, 2006, Wine Co. sent information to all its clients stating that it was offering its entire production in the vineyard for 2006 but that the price could not be lower than US $6 per bottle, and its entire production was approximately three million bottles. In addition, Wine Company advised that clients interested in buying the production would have to respond by communication sent to Piero Monestier, CEO of the company no later then January 30, 2006 and that a final contract should be signed by March 30, 2006, after the inspection and testing of the product by interested buyers. The inspection was programmed for February 16, 2006. Three South American firms expressed interest: Concha Co. from Colombia; Toro from Chile and Tinto from Argentina. These three clients traveled to Italy for the inspection. The inspection was held for four days and the clients brought specialists to determine the quality of the wine. The contract was to be awarded to the best proposal twenty days after of the inspection. However, Wine Co. informed its clients ten days after the inspection its refusal to continue with the negotiations. Wine Co. did not give any specific reason to its clients. The company only indicated that due to a policy of the company the negotiation was canceled. Wine Co. knew since January 30, that the negotiation would be canceled due to their contractual obligation with an Italian client. However, the Company did not stop the negotiations and continued with them until the inspection and then, only a few days before the award of the contract, withdrew its proposal. All the countries involved in the negotiations had their relevant places of business in countries that subscribed to the CISG. The damages caused to the clients included the loss of out-of-pocket expenses and the loss of opportunities because they refrained from negotiating with other providers due to the ongoing negotiations with Wine Co.

To establish a case under the concept of pre-contractual liability, four elements are required:[32]

[32] Novoa, *Supra* note 27, at 583

1. *"Preliminary negotiations;*
2. *Breach of the duty to bargain in good faith;*
3. *Causation in fact; and*
4. *Compensable damages."*

The hypothetical case meets these requirements. There were preliminary negotiations, (the requirement of prior inspection of the product and the posterior communication of the offer after 20 days of the inspection), Wine Co. without justification and in bad faith withdrew the negotiations and, as a consequence of the rupture of the negotiations, its clients suffered damages in reliance on its statement and conduct. Wine Co. promoted the preliminary negotiations and did not withdraw the negotiations, as soon as it found out that such a contract would not be concluded. The Company continued with the inspection and let the clients invest money in their travel expenses, salary of experts and caused them to miss other opportunities.

In situations as illustrated in this hypothetical case the application of pre-contractual liability under the CISG should be possible. First, the CISG promotes the general principals of good faith and fair dealing. Therefore, it is possible to conclude that the parties, since the beginning of the negotiation, have the obligation to bargain in good faith and the breach of such obligation will render legal consequences for the damages caused by the breach. Also, it is reasonable to conclude that a party, in reliance on the other party's promises, statements or conduct, will proceed with the due diligence that was required to obtain the conclusion of the contract. For instance, in the hypothetical example any reasonable person in the same situation would have understood that Wine Co. had a serious intention to conclude the negotiations and award the contract to the best offer (Article 8). The parties would never incur such investment in money and work if they did not have an understanding that the proposal sent by Wine Company was serious. Therefore, the intention of the parties was clear. The Wine Company showed an intention to conclude a contract. It would be unfair to conclude that the parties should pay for the cost of the inspection and travel because Wine Company required them to execute the inspection as a condition precedent before the awarding of the contract under circumstances in which. Wine Company knew its intention to withdraw the negotiations but failed to communicate this determination in time. Wine Company did not act according the general principles of good faith and fair dealing that inspire the CISG.

Conversely, I would like to think of the outcome of this case under the analysis of the majority view that held that pre-contractual liability is outside of the scope of the CISG. In their analysis they will probably indicate that the domestic law would apply instead of the CISG because the Convention is silent to this respect.

In my opinion, regarding pre-contractual liability as outside the scope of the CISG will lead to uncertainty and ambiguous interpretations and outcomes because the gap will be fulfilled according to the provisions of the domestic laws. Therefore, if a pre-contractual liability case is decided in common law jurisdictions, it is likely that the parties will not be allowed to recover damages for the unjustified withdraw of pre-contractual negotiations. Conversely, if the same case is resolved by a judge in the civil law jurisdiction, the innocent party will likely be allowed to recover the damages caused in reliance on the other party's intention to conclude a future contract. In consequence, the innocent party will be compensated for the cost of expenses and the lost of opportunities suffered during pre-contractual negotiations.

I believe that the application of domestic law in cases of pre-contractual liability in international contracts would infringe the major principals and goals of the CISG because it will be a lack of unity in the interpretation and outcomes in this matter. Therefore, this conclusion would not honor the uniformity and unity that the Convention pursues.

C. Comparison Between the Application of Pre-Contractual Liability Under the CISG and Colombian Domestic Law

Colombian legislation regulated pre-contractual liability under the Civil and Commercial Code. In contrast, the CISG is silent respect to this matter. The majority of the scholars opine that pre-contractual liability is not within the scope of the CISG. However, I believe that pre-contractual liability is regulated under the CISG and is not outside its scope.

As I indicated before, it is possible to infer its application through the interpretation of its general principles and provisions as a whole. In consequence, the application of pre-contractual liability is possible under the interpretation of the regulations provided in articles 7 and 8 of the CISG.

Article 7 regulates the international character of the Convention and provides for the promotion of good faith in international trade. In addition, this article indicates that where a matter is governed by the Convention but not expressly settled in it, the correct approach is to resolve the matter according to its general principles, where such principles are present.

Similarly, Article 863 of the Colombian Commercial Code sets forth the obligation of the contracting parties to act in good faith and without fault during pre-contractual negotiations and provides that the failure to comply with this obligation will cause the liability of the party at fault.

In addition, Article 872 of the Commercial Code indicates that the celebration and execution of the contracts shall be in good faith.

Moreover, the CISG in Article 8 states that the intention, statements and conduct of the contractual parties should prevail in the interpretation of the contract.

In this aspect, the CISG is also similar to the Colombian legislation because Article 1618 of the Colombian Civil Code states that, once the intention of the contractual party is known, that intention prevails against the literal interpretation of the provisions of the contract.

Finally, both legislations will award damages in reliance to the innocent party. In both cases, the innocent party will be compensated for his out-of-pocket expenses and lost opportunities.

It is also important to mention that, under article 16(2)(b), the CISG regulates promissory estoppel. According to this article, an offer can be withdrawn at any time before its acceptance except when is reasonable to believe that the offeree *in reliance on the offer* acted in a certain way. For instance, the party commenced investment in production, hired some employees and invested in infrastructure, and as a consequence, will suffer damages if the offer is revoked. Thus, he should be allowed to recover damages in reliance. In my view, this protection can be extended to pre-contractual agreements because we are facing similar situations. In pre-

contractual negotiations, we have a party who acted in reliance on the negotiations and as a consequence researched the business, invested money and time learning the opportunities and benefits of the future contract. Therefore, in case of an unjustified withdraw of the negotiations the blameworthy party should be held responsible for the damages caused in reliance.

IV. CONCLUSION

It is true that there is no provision in the CISG that specifically regulates pre-contractual liability. In this respect, the CISG is silent. However, its application can be inferred from its general principles and provisions and from the interpretation of the Convention as a whole. As stated before, the first step is to look to article 7(1), which indicates the international character of the Convention and its promotion of the principal of good faith in international trade. In addition, article 7(2) indicates that where a matter is governed by the Convention but not expressly settled in it the correct approach is to resolve the matter in accordance with the general principles of the Convention where such principles are present.

In my opinion, the intention of the drafters of the CISG was to bind the contracting parties to the compliance of good faith since the beginning of the negotiations of the contract of sale.

Furthermore, one must analyze the intention of the contracting parties according to Article 8. The questions that may arise are: Was there an intention to conclude a contract? Where there promises, statements or conduct that would lead the other contracting party to infer the conclusion of a contract and therefore proceed with the researching the business? If these questions are answered in the affirmative, then it is possible to infer the application of pre-contractual liability due to the reliance of one party in the other's statements and conduct.

Moreover, I think that the UNIDROIT provision on bargaining in good faith could be extended to the CISG because the interpretation of the general principles of the convention should be broader and not only limited to the general principles derived from the Convention. Thus, it could be sustained that the principles of the UNDROIT and PECL can be used as a source of the general principles provided in Article 7(2) CISG as it have been sustained by Salama's theory.